Distr.
GENERAL

IDB.26/3
PBC.18/4
20 June 2002

United Nations Industrial Development Organization

ORIGINAL: ENGLISH

## Industrial Development Board

Twenty-sixth session
Vienna, 19-21 November 2002
Item 2 (a) of the provisional agenda

## Programme and Budget Committee

Eighteenth session
Vienna, 24-25 September 2002
Item 3 of the provisional agenda

# REPORT OF THE EXTERNAL AUDITOR, FINANCIAL PERFORMANCE REPORT AND PROGRAMME PERFORMANCE REPORT FOR THE BIENNIUM 2000-2001

**Comments of the Director-General on the report of the External Auditor**

1. The present document provides the Director-General's comments on the report of the External Auditor covering the period 2000-2001 (PBC.18/3-IDB.26/2).

### I. GENERAL COMMENTS

2. The Director-General takes note of the report, which contains useful analyses, observations and recommendations, and notes that the comments of the Secretariat on the draft report have largely been taken into account in the External Auditor's report.

3. The Director-General is pleased to note the following concluding assessment made by the Auditor, which provides an independent confirmation on the achievements of the transformation process initiated by him in December 1997, upon commencement of his term as Director-General of UNIDO (PBC.18/3-IDB.26/2, para. 136):

> "During my term of office of eight years, I have witnessed the severe difficulties faced by the Organization as to its raison d'être, as well as the resulting uncertainty faced by its staff until the end of 1997. Since then, Member States, Management and the Organization's staff have jointly worked hard to reverse this trend and regain the confidence of the international community. I am now pleased at this point in time to report that the Organization has achieved relevance, financial stability, improved technical cooperation delivery and quality of services offered through more focused activities. The future looks promising for UNIDO. My staff and I would like to take this opportunity to extend our good wishes for the future to the Organization and its staff."

4. The Director-General is grateful to the External Auditor and the audit team for their constructive suggestions for improving the economy, efficiency and effectiveness of the financial procedures, the accounting system, the internal financial controls and, in general, the administration and management of the Organization, as called for under financial regulation 11.4. The Auditor's contribution in the following areas over the past four years is particularly worth mentioning: the introduction of the euro; rationalization of major objects of expenditures; an exchange rate for the conversion of

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V.02-55513 (E)

Distr.: 24 July 2002

assets, liabilities, reserves and fund balances as a result of the introduction of the euro as a single currency; special accounts for Buildings Management and Regular Programme of Technical Cooperation; and the implementation of the new financial system. The Director-General has always valued greatly the recommendations made by the Auditor and has endeavoured to implement them to the extent possible, which is confirmed by the Auditor in paragraph 126 of his report: "Initially the assessments and recommendations in the Audit Observations did not always receive a warm welcome ... I am generally pleased with the action taken by the Organization in these cases, most of these by the current Director-General."

5. The Director-General also wishes to record his sincere appreciation for the excellent work of the entire audit team since the initial appointment in 1994 of the President of the Federal Court of Audit in Germany as the External Auditor of UNIDO. As stated above, the high standards of the External Auditor and the audit team since their appointment have contributed in no small measure to the work of UNIDO.

## II. SPECIFIC COMMENTS

**Implementation of the regular budget and technical cooperation** (paras. 5-14)

6. The comments of the Auditor on the improved collection rate of assessed contributions and arrears; on the distinct drop in the unencumbered balances of appropriations (i.e. 96.4 per cent implementation of the approved regular budget); on improved technical cooperation delivery in 2001 and the positive outlook for future years have been noted with satisfaction.

**Financial situation** (paras. 15-24)

7. The Director-General notes with satisfaction the Auditor's comments that UNIDO's financial situation as well as the Special Account for Programme Support have stabilized in recent bienniums.

**Budgeting, accounting and financial reporting procedures** (paras. 25-50)

8. As pointed out by the Auditor, a major challenge for UNIDO's financial management in 2000-2001 was the implementation of the new Financial Performance Control System (FPCS), which was implemented by the Organization within its own limited resources, in contrast to the usual approach to rely heavily on external resources and consultants. As a result, the first phase of the FPCS was achieved at a considerably lower cost (approximately $1.7 million) and in less time than in other organizations. The Audit team's contribution during the implementation of the system, in particular during the reconciliation of the old and the new systems, was greatly appreciated.

9. The staffing constraints faced by the Financial Services Branch, as noted by the Auditor, have been largely addressed with the recent recruitment of junior Professionals.

10. The Director-General also notes with satisfaction that a complete check of all cash accounts and bank statements, as well as a comprehensive sample checking of accounting entries and other checks carried out by the Auditor during the years 2000, 2001 and 2002 did not disclose any material errors in UNIDO's accounting, thus enabling the Auditor to express a clear audit opinion on the financial statements for biennium 2000-2001.

**Women in the Secretariat** (paras. 51-52)

11. The Director-General has always shared the concerns of the Auditor with respect to the representation of women in the Secretariat. As acknowledged by the Auditor, the Director-General has made considerable efforts to improve both the representation of female Professional staff and the geographical representation, in particular with the recruitment drive of 2001. In future recruitment, the Director-General will continue to pay close attention to this issue.

**Technical cooperation activities** (paras. 53-99)

12. The comments of the Auditor have been noted regarding greater use of subcontracting and package deals with suppliers. These will be taken into consideration, bearing in mind the provisions of the Financial Regulations and Rules of UNIDO and other guidelines covering the implementation of technical cooperation programmes and projects.

13. As noted by the Auditor, a number of comments in the report lie outside the control of UNIDO, including donor community policies and requirements, decentralization by donors contributing to additional administrative requirements on UNIDO's part, the establishment of a non-specific project fund, and assistance to some economically non-viable enterprises. However, the Secretariat will bear these recommendations in mind in the design of future programmes and projects and will negotiate with donors as appropriate.

14. The Director-General has also noted the Auditor's recommendation on the implementation of a code of ethics and especially a staff rotation concept in areas that are by nature fraud endangered. A United Nations system-wide code of ethics which has just been updated by the International Civil Service Advisory Board will

soon be brought to the attention of all staff. At the same time, and as pointed out by the Auditor, upon initial appointment all staff sign an oath of office concerning their conduct as international civil servants as contained in staff regulation 1.8. Regarding staff rotation, the Director-General has initiated a system of rotation between Headquarters staff and the field, and this recommendation will be taken into account in future reassignments.

**Administrative issues and other matters**
(paras. 100-137)

15. The Director-General has taken note of the recommendations of the Auditor regarding improved stock-taking procedures, an evaluation of global forum activities, the development of measurable performance indicators and reflections and future direction. Chapter V of the Annual Report 2001 provides information on UNIDO's development of performance indicators based on the best currently available in the public and private sectors. Work is now being focused on the implementation of a balance scorecard that aims to integrate four interdependent sets of measures associated with UNIDO's corporate strategy: customer satisfaction; internal processes; innovation and learning; and financial. Due attention will be given to implementing these recommendations.

16. With regard to the recommendations concerning the After-Service Health Insurance (ASHI) liabilities (para. 114 of the Auditor's report), the Secretariat's position is that a system-wide approach would be more appropriate than a stand-alone solution by UNIDO. As noted by the Auditor, the High-Level Committee on Management is considering this issue, and some other organizations have begun to reserve funds for such purposes, or plan to do so in the future. As recommended by the Programme and Budget Committee in conclusion 2000/2, an actuarial study to determine the financial impact of ASHI was carried out which shows the present level of unfunded liabilities to be $39.4 million (document PBC.17/9 refers). Member States and the Secretariat need to find a solution to address this issue.

## III. ACTION REQUIRED OF THE COMMITTEE

17. The Committee may wish to consider recommending to the Board the adoption of the following draft decision:

"The Industrial Development Board:

"(a) Takes note of the report of the External Auditor on the accounts of the Organization for the financial period 2000-2001 (PBC.18/3-IDB.26/2);

"(b) Also takes note of the Director-General's comments on the report of the External Auditor (PBC.18/4-IDB.26/3);

"(c) Expresses its appreciation and gratitude to the President of the Federal Court of Audit of Germany and the audit team for their valuable contribution to improving the operations of UNIDO during the period 1994 to 2002;

"(d) ..."